IN THE

Supreme Court of the United States

OCTOBER TERM, 1902

No. 301

D. N. HOLDEN AND LIZZIE HOLDEN, Appellants,

vs.

JAMES A. STRATTON, TRUSTEE, Appellee.

STATEMENT OF THE CASE.

In January 1901, The First National Bank of Seattle, Washington, filed in the United States District Court, for the District of Washington, Northern Division, its petition setting forth that petitioner was a creditor of Daniel N. Holden and Lizzie Holden, his wife, that said Holdens were insolvent, and praying that they be adjudged to be bankrupts within the purview of the Acts of Congress relating to bankruptcy.

Said Holden and wife in answer to said petition admitted

their insolvency and prayed to be adjudged bankrupts. Thereafter they were duly adjudged bankrupts, and James A. Stratton, Esq., was duly elected and qualified as trustee in bankruptcy of their estates under the laws of the United States. Subsequently appellants claimed among other property exempt under the State law certain policies of life insurance which had been delivered to the trustee. These policies were issued on the 15th of June, 1894, by the Northwestern Life Insurance Company of Milwaukee, Wisconsin, and are numbered respectively 206,383, for $5,000.00; and 303,921 for $2,000.00. In both, Daniel N. Holden is the insured and Lizzie Holden, his wife, is named as the beneficiary. (The policies, according to the claim of trustee, if allowed, have a present combined cash surrender value of about $2,200.00. That they have any cash surrender value, we deny. This is one of our contentions.)

The Referee in Bankruptcy, Hon. John P. Hoyt, ex-Chief Justice of the Supreme Court of the State of Washington, ruled on June 17th, 1901, that said policies were not exempt, but passed and were vested in the said trustee. But the Referee in his certificate disallowing the exemption added, "In justification of said ruling, I desire to state and certify that if this question had been in my opinion, an open one in this circuit, I should have held that said policies of insurance were, under the term of said Bankrupt Laws, exempt to the Bankrupts and did not pass to the trustees; but the court of Appeals of this Circuit, having in the case of *In re Scheld, 104 Fed. 870*, passed upon this question and there being in my opinion no reason for distinguishing the case at bar from the above cited case, I feel bound to decide and certify as above stated. As Referee I do not feel that I would be justified in attempting to distinguish that case from this one, nor to make a ruling without regard thereto even although I am satisfied that the Court, in deciding said case improperly interpreted the bankrupt law of the United States."

On July 16th, 1901, the District Court after an exhaustive presentation of the issue by counsel for appellant and appellee, entered an order setting aside the action of the Referee and directing that said policies be turned over to appellants as exempt. Whereupon, appellee applied to the United States Circuit Court

of Appeals for the Ninth Circuit for a revision and review of the said order of the District Court to the end that the claim of exemption of appellants be denied and the action of the lower Court corrected. The case is now in this Honorable Court upon the appeal of said bankrupts from the decree of the said Circuit Court of Appeals setting aside the said order of the District Court, and declaring said policies to be not exempt.

ASSIGNMENT OF ERRORS.

Appellants make the following assignment of errors in the opinion and decree of the honorable Circuit Court of Appeals, filed respectively in said Court on the 6th, and 16th day of January, A. D. 1902, to-wit:

FIRST. It was error to find and hold that the Life Insurance Policies issued to Daniel N. Holden on the 15th day of June, 1894, and numbered respectively 206383 and 303921, for the respective sums of $5,000.00, and $2,000.00, were not exempt under the Bankrupt Law.

SECOND. It was error to order that the decree of the District Court allowing said Bankrupts claim of exemption, be set aside.

THIRD. It was error not to find and hold that said Policies of Insurance and the proceeds thereof, were exempt under the Bankrupt Act, from all claims of the creditors of said Bankrupts.

POINTS AND AUTHORITIES.

In the year 1897, the Legislature of the State of Washington enacted "That section one of an act entitled 'An act exempting the proceeds of Life Insurance from liability for debt, and declaring an emergency,' approved March 20, 1895, is amended as follows:

"SECTION 1. That the proceeds or avails of ALL life and accident insurance shall be exempt from all liability for any debt.

"SECTION 2. An emergency exists, and this act shall take effect immediately."

LAWS OF WASHINGTON 1897, PAGE 70.

It is stipulated by appellants and appellee "That all and every of the liabilities of said bankrupts were made and contracted between the first day of September, 1900, and the first day of December, 1900.

See Record, Page Abstract 3.

In 1898 Congress passed the Bankrupt Act, Section 6 of which declares:

"This act shall not affect the allowance to bankrupts of the exemptions which are prescribed by the state laws in force at the time of the filing of the petition in the state wherein they have had their domicile for the six months or the greater portion thereof immediately preceding the filing of the petition." But section 70 of the act reads as follows:

"The trustee of the estate of a bankrupt upon his appointment and qualification, and his successor or successors, if he shall have one or more, upon his or their appointment and qualification, shall in turn be vested by operation of law with the title of the bankrupt, as of the date he was adjudged a bankrupt, except in so far as it is to property which is exempt; to all (1) documents relating to his property; (2) interests in patents, patent rights, copyrights and trade-marks; (3) powers which he might have exercised for his own benefit, but not those which he might have exercised for some other person; (4) property transferred by him in fraud of his creditors; (5) property which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him; provided, that when any bankrupt shall have any insurance policy which has a cash surrender value payable to himself, his estate, or personal representatives, he may within thirty days after the cash surrender value has been ascertained and stated to the trustee by the company issuing the same, pay or secure to the trustee the sum so ascertained and stated, and continue to hold, own, and carry such policy free from the claims of the creditors participating in the distribution of his estate under the bankruptcy proceedings, otherwise the policy

shall pass to the trustee as assets; and (6) rights of action arising upon contracts or from the unlawful taking or detention of or injury to, his property."

The question then is, does the provis o in section 70 negative the absolute and unqualified rule of exemption as declared in section six, to-wit: the State law? We believe not, for as was said by Caldwell, Circuit Judge, in *Steel V. Buel*, (*104 Federal Reporter, page 968.*)

"This section (sec. 6) establishes the rule of exemption in the most absolute and unqualified terms, and that rule is the state law. * * * This rule of exemption, therefore, pervades the whole act, and is to be read into every other section and provision of the act. If Congress had intended to diminish or lessen the state exemptions in any case, and particularly if it had intended to subject to the payment of the bankrupt's debts his policies of life insurance which were exempt under the state law, that intention would undoubtedly have found expression in clear and unmistakable language in Section 6. That was the appropriate place for limiting or qualifying the state exemptions, if it was to be done at all. * * * How is it to be known what "is exempt?" There is but one source of information on that subject, and that is the state law adopted by Section 6, and the legal effect of this section is precisely the same as if it read, "except property which is exempt under the state law." This exception must be read into every other clause and provision of the section. The fifth clause of this section shows conclusively that the construction of the proviso contended for by the trustee is wholly inadmissible. By the plain language of this clause of this section, the trustee is invested with a title to all the bankrupt's "property which prior to the filing of the petition he could by any means have transferred * * *." Now, the bankrupt could have transferred every particle of property he owned prior to the filing of the petition, and why does not the trustee set up a claim to all of it under this clause? Because it is felt that if such a claim was made it must fail, for the reason that it would be preceived at once that to grant it would completely nullify section 6, and all exemptions under state laws leaving the bankrupt without any

exemption whatever. But there is just as much reason for the trustee claiming under this clause all the property exempt under the state law as there is for claiming a part of it. The difference is one of degree only. It is obvious that section 6 must be read into this clause, if that section is to have any effect at all, and the bankrupt to be allowed any exemptions. But the clause of the fifth paragraph immediately preceding the proviso, and to which the proviso, according to the accepted rule for the construction of provisos, must be referred, removes all doubt as to what is meant by the proviso. In connection it reads: "The trustee * * * shall be vested by operation of law with the title of the bankrupt * * * to all property which might have been levied upon and sold under judicial process: provided, that when any bankrupt shall have any insurance policy which has a cash surrender value," etc. What kind of an insurance policy is here meant? Plainly and obviously an insurance policy "which might have been levied upon and sold under judicial process," and as to such policies the proviso makes a provision by which the bankrupt may retain his policy by paying its cash surrender value, and thus retain the benefit of the low rate of premium obtained when he was younger, and which could not be obtained upon a new policy. Moreover, the proviso is to be read in the light of section 6, and made to harmonize with it and other provisions of section 70, and, giving due effect and operation to this rule of construction, the proviso means precisely what it would if it read, "provided, that when any bankrupt shall have any insurance policy *not exempt*." The italicized words or their equivalent are necessarily implied from the other provisions of this section as well as from the sweeping provisions of section 5, and what is implied in a statute is as much a part of it as what is expressed.

U. S. v. Babbitt, 1 Black 61, 17 L. Ed. 94; Gelpcke v City of Dubuque, 1 Wall. 221, 17 L. Ed. 519; Wilson Co. v. Third Nat. Bank, 103 U. S. 770, 26 L. Ed. 488; Thurber V. Miller, 32 U. S. App. 209, 14 C. C. A. 432, 67 Fed. 371.

"This construction gives effect to every provision of the act, and renders them harmonious."

The honorable Circuit Court of Appeals for the Ninth Circuit in *In re Scheld, 104 Fed. Reporter, 870*, being the decision referred to by Referee Hoyt, in his said certificate in this cause to the District Court, and by his honor, Justice McKenna, in the decision of this cause in the Court of Appeals, held that the proviso in section 70 is a specific limitation on section 6, and that the title to Life Insurance policies having a cash surrender value vests in the trustee, notwithstanding the exemption under the state laws.

In the Scheld case, the Court of Appeals does not make any extended analysis of the bankrupt act, but simply lays down the broad proposition that "the fact that this special clause is preceded by the word 'provided' does not in any sense limit the force thereof," citing

Railroad Co., vs. Smith, 128 U. S. 174.

But that part of R. R. vs. Smith, in regard to the term "provided" is mere *obiter dictum*, and was in no way necessary to and was not considered as a ground for the decision. And certainly the learned court in the Scheld case did not take into consideration the policy of Congress to always exempt to debtors and bankrupts the property exempt to them by the State law; nor, to give to the bankrupt act such a construction as would give effect to each and every part thereof. It seems a forced construction to say that "giving to the words used in section 70 their usual and fair import, they clearly declare that policies of insurance of the character of that in issue in this case pass to the trustee as part of the assets of the bankrupt."

In the Scheld case, the Court cites in *Re Lange (D. C.) 91, Fed. 361*, in support of their position, that the policies were not exempt. The doctrine in the Lange case was also urged but overruled in Steele vs. Buel, supra, for as is therein stated "the District Court, somewhat doubtedly, confirmed the ruling of the referee, on the authority of a previous decision of that court in *Re Lange (D. C.) 91 Fed. 361*, and thereupon the bankrupts appealed the case to this court." Judge Shiras, who decided the Lange case, afterwards in *In Re Steele 98 Fed. 79*, said: "

"I freely admit that the question (as to said exemptions) is not

free from doubt." Thus showing an additional weakness in the position taken by the Court in *Re Scheld*, which case is made decisive of the case at Bar.

Again, citing from *Steele vs. Buel, supra.*

"It has always been the policy of congress to exempt to debtors and bankrupts the property exempt to them by the state law. From the organization of the federal courts under the judiciary act of 1789, the law has been that creditors suing in those courts could not subject to execution property of their debtor exempt to him by the law of the state.

Judiciary Act 1789 (1 Stat. 93, c 21); Wayman v. Southard, 10 Wheat. 1, 32, 6 L. Ed. 253; Lamaster v. Keeler, 123 U. S. 376, 8 Su. Ct. 197, 31 L. Ed. 238; Dartmouth Sav. Bank v. Bates (C. C.) 44 Fed. 546.

"Confessedly, the creditors, who through the trustee are now seeking to subject these policies to the payment of their debts, could not have subjected them to the payment of their debts by execution or other legal process issuing either from the state or the federal courts. The same rule has obtained under the bankrupt acts, which have sometimes increased the exemptions, notably so under the act of 1867 (section 5045, Rev St.), but have never lessened or diminished them. An intention on the part of congress to violate or abolish this wise and uniform rule observed from the creation of our federal system should be made to appear by clear and unmistakable language. It will not be presumed from a doubtful or ambiguous provision fairly susceptible of any other construction. If congress was going to attack the state exemptions and lessen or diminish them in any degree, the exemption of life insurance policies would be the very last exemptions to be attacked. They are very generally esteemed the best and safest means by which a man of limited means, or one dependent on his daily earnings for his support, can make provision to preserve his family from suffering and want after his death. This is the view taken of life insurance policies by the supreme court of the United States. * * * Instead, therefore, of nullify-

ing the fundamental and basic rule of exemption established by section 6, and curtailing the exemption under the state law, the proviso in question was intended to and does give the bankrupt a right which, in states whose laws do not exempt policies of life insurance, he would not have without it. The proviso is operative in those states only whose laws do not exempt them. This construction removes all seeming conflict or inconsistency between section 6 and the proviso of section 70, and gives that effect to each which congress plainly intended they should have."

But for the sake of argument, suppose the proviso in section 70 limits the rule of exemptions as laid down in section 6. The question then arises, "do the two Holden policies come within the definition of policies having a cash surrender value?" The term "cash surrender value," as used in the Bankrupt Act, means the cash value—ascertainable by known rules—of a contract of insurance abandoned and given up for cancellation to the insurer by the owner, having contract right to do so.

In re Welling (U. S. C. C. A.) 113 Fed. 189.

In the case at bar, policy No. 303921, for $2000.00, is a non-participating paid-up policy, payable in case of death to Lizzie Holden, the beneficiary therein named. The policy does not contain any provisions as to surrender, nor options. In other words it does not come within the above definition. For as was said in Re Welling (Supra). "The surrender of the proviso is not the subject of negotiation or agreement, but of right. The proviso does not include those policies where the right to surrender is not given by the contract." And in the present case, as in the Welling case, surrender could only be legally accomplished through agreement with the company by the joint action of Holden and his wife. There exists no right in either the wife or husband, jointly or singly, to surrender. It could only be done by the joint action of the two by agreement with the assurance society. But in the Welling Case the court went further and found that while the policy did not fall within the terms of the proviso, the bankrupt had property therein which passed to his trustee, for by the terms of the policy in that case the bankrupt

was entitled to receive at the end of the tontine period the cash payment stipulated in the contract. But in the case at bar, the policy under consideration (No. 303921) does not give any vested contract rights as to any cash payments upon any dates certain, no payment being stipulated for except the $2000.00 upon the death of the insured. Hence, in Re Welling directly sustains our position as to the exemption of said policy No. 303921.

Let us now consider the other Holden policy, No. 206383, for $5000.00. The company by this contract agrees that, upon the payment of $233.80 on the 21st day of May in every year during the first ten years from May 21st, 1890, it will pay the said insurance to Lizzie Holden, wife of D. N. Holden, the insured, within sixty days after due proof of the fact and cause of the death of said insured. The premiums have all been paid. The policy contained the statement that it is issued on the Semi-Tontine Plan, and its Tontine Divided Period is twenty years, and that the policy shall share in the Surplus, according to company's usage, at each distribution after twenty years from May 21, 1890. There is endorsed upon the policy certain options which the insured may have upon the completion of the Tontine Dividend Period. The policy does not provide for any cash surrender value. Therefore, according to the Welling Case, it does not fall within the provisions of section 70 of the Bankrupt Act relating to a cash surrender value. But in that case, the Court held that though the policy had no "cash surrender value," within the meaning of the proviso, it had an actual value, which constituted a right of property in the bankrupt, and which could have been transfered by him. And therefore passed to the trustee. In the Welling Case the law of the state of the domicile of the bankrupt *does not* exempt policies of insurance. But we review it here to show to your Honors that even where the question as to the construction to be given to the proviso is not raised, there is much difference of opinion as to just what life insurance policies do pass to the trustee. After careful study of the case of in Re Welling, we are firmly convinced that the dissenting opinion of Circuit Judge Grosscup in that case states the law correctly, and that this Honorable Court can directly see the force and

logic of his position, we cite therefrom the following:

"* * * Another term of the option is (as in the case at bar) that the election shall be by the husband himself. No one else can stand in his place, or exercise the option under the circumstances and sense of obligation that would influence him. * * * I am of the opinion that a fair interpretation of the spirit of the policy would disallow the exercise of the option of Welling until the day for its exercise had arrived, and would then disallow its exercise, unless it be by the judgment of Welling himself. Such an interpretation, of course, forbids the view that the option is transferable in advance—in this case six years in advance—or was subject to levy by creditors."

If in the Welling case the option is not transferable six years in advance' how much more reason there is that in the case at bar, it should not be transferable ten years in advance, and especially as no definite sum is guaranteed in the Holden policy to be paid upon its surrender at the completion of the Tontine Dividend Period.

It may not be out of place to refer here to the case of *In Re Heilborn's Estate, 14 Wash. P. 536,* Cited by Justice McKenna in the opinion filed in the Circuit Court of Appeals in this case. In the Heilbron case the policies were made payable to Heilbron's executors in case of his death. By the terms of his will, his brother W. C. Heilbron was bequeathed of the sum of $5,000.00. Other legacies were bequeathed by the deceased. ~~The brother, W. C. Heilbron was bequeathed the sum of $5,000. Other legacies were bequeathed by the deceased.~~ The brother of C. W. Heilbron assigned his interest to the Guarantee Loan and Trust Co. of Seattle. According to opinion of the Supreme Court of Washington, it appears that George H. Heilbron died insolvent, and was insolvent at the time of making the will. In that case it argued, according to the opinion of the court, that the policies of insurance belonging to the estate were liable for the debts of the deceased; that these debts were incurred prior to the enactment of the law exempting the policies of life insurance from liability for debt. The Holden policies are not payable to the executors of the estate. In the Heilbron case, the estate of the deceased became the ben-

ificary, and afortiori the creditors. In this case the wife is made the beneficiary and the policies are only payable upon conditions precedent, and these conditions precedent require the concurrence of three wills, and these conditons or concurrence may be in the future, in fact must be in the future, that is leaving out the question of death. Three minds must agree before anything can be had from the policies until the consummation of a time certain and fixed in the policies. Can the creditors in this case, through their trustee, force a concurrence of minds? Can they compel the Insurance Company, against its will, to shorten the time fixed in the policies? In other words, can the trustee destroy the object of the insurance and so destroy or annul the benevolent act of the state?

Should this Honorable court hold that the policies here in issue are not exempt under the Bankrupt Act, the question would then arise: has congress the power to abrogate state exemption laws?

Whatever is not conferred in the Constitution is withheld. and belongs to the several states, or to the people thereof.

Cooley's principles of Constitution Law, p 29.

Any enactment of Congress which is opposed to the provisions of the Constution, or is not within the grant of powers made by it, is unconstitutional.

Idem. p. 31.

Hence, as no such grant of power has been made to it, Congress has never claimed the right to abrogate state exemption laws.

In re Beckerford, 1 Dillon 45.

Nor is any such right properly an incident to an expressed power in the constitution, and necessary to its execution.

But to give the exemption phase of the Bankrupt Act the construction contended for by the Trustees, and as laid down by the Circuit of Court of Appeals, would in effect be giving to Congress the unauthorized power to abrogate and annul state exemption laws.

We beg your Honors' indulgence while we discuss this feature of the case a little further. Under Art. I Sec. 8, among other powers, Congress has the following: "To estabish an uniform

rule of naturalization, and uniform laws on the subject of bankruptcies throughout the United States." And here let us not forget that ours is a Republican form of government, or in other words, an agreement of the people, for the people, and by the people; A constitutional democracy.

This is implied by articles 9 and 10 of the amendments. The Constitution reads thus: (Art. 9.)—"The enumeration in the Constitution, of certain rights, shall not be construed to deny or disparage others retained by the people." (Art. 10.)—"The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people." Here then is a limitation on the powers of Congress. It seems to us it cannot be successfully argued that the State has not reserved the power to legislate, within its own sovereign domain, for the people claiming citizenship, personal and proper rights within the Commonwealth. The state in its beneficence has seen proper to exempt among other property, from liability for debt, life insurance.

"That the power to tax involves the power to destroy; that the power to destroy may defeat and render useless the power to create; that there is a plain repugance in conferring on one government a power to control the constitutional measures of another, which other, in respect to those very measures, is declared to be supreme over that which exerts the control,—are propositions not to be denied."

Cooley on Principles of Constitutional Law, 61. McCulloch v. Maryland, 4 Wheat. 316, 431.

"It is true that taxation does not necessarily and unavoidably destroy, and that to carry it to the excess of destruction would be an abuse not to be anticipated; but the very power would take from the States a portion of their intended liberty of independent action within the sphere of their powers, and would constitute to the State a perpetual danger of embarrassment and possible annihilation. The Constitution contemplates no such shackles upon state power, and by implication forbids them.

Cooley, Id, p. 62.

The power of the States to protect the lives, health, and property of their citizens, and to preserve good order and public morals is a power originally and always belonging to the states, and not surrendered by them to the general government.

United States v E. C. Knight Co., 156, U. S. I.

If then the power of the State to protect the lives, health and property of its citizens, and to preserve good order and public morals, is a power originally and always belonging to the state and has not been surrendered by it to the general government, how will Congress undertake within the constitution to annul and abrogate a law exempting the property of a citizen from liability for debt?

While Congress has a right to enact the Bankrupt Law and make it uniform throughout the United States, still we have seen that that uniformity does not consist in exemptions, for many of the States differ in their exemption laws, and notwithstanding this difference, which is in a measure the lack of uniformity, the Bankrupt law has been held by this Honorable Court to be constitutional while this non-uniformity has existed. Again we put the question to your Honors, has Congress the power to abrogate and destroy the exemption laws of a state? Is that not a law regulating property rights?

Respectfully Submitted.

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